

CARRIX, INC.

**SUBMISSION OF WRITTEN COMMENTS FOR THE HEARING RECORD
U.S. HOUSE OF REPRESENTATIVES
COMMITTEE ON WAYS AND MEANS**

**HEARING ON THE NEED FOR COMPREHENSIVE TAX REFORM
TO HELP AMERICAN COMPANIES COMPETE IN THE GLOBAL MARKET
AND CREATE JOBS FOR AMERICAN WORKERS**

MAY 12, 2011

Mr. Chairman, Ranking Member Levin and distinguished Members of the Committee:

Carrix, Inc. (“Carrix”) is pleased to submit written comments for the record in connection with the May 12, 2011 hearing of the Committee on Ways and Means (“the Committee”) on the critically important topic of reforming our nation’s international tax laws. Carrix is a U.S.-based ***closely held*** port terminal operating company that manages more cargo terminals than any other company in the world. Carrix provides a full spectrum of transportation services – from terminal management to stevedoring – in a number of U.S. and foreign ports.

As a company built on international trade, Carrix fully appreciates the topic of today’s hearing: reforming our international tax laws to make U.S. companies more competitive vis-à-vis their foreign competitors. Carrix, like many other U.S.-based companies in all sectors of the economy, faces fierce competitive pressure from foreign-based companies. Unlike most other U.S.-based companies, many of our foreign-based competitors are large foreign multinationals, some of which are closely aligned with foreign governments, and operate under more favorable home country tax regimes.

We would like to bring to the Committee’s attention a tax issue that directly and negatively impacts our ability to grow our U.S. operations: the potential application of the personal holding company (PHC) tax to earnings we would seek to repatriate in the form of dividends from our foreign subsidiaries. As will be discussed further, the PHC tax is an outmoded relic in the Tax Code that offers little, if any, compelling policy rationale for its continued existence. As the Committee considers fundamental tax reform, we believe the regime should either be repealed or substantially revised.

Background on the Personal Holding Company Tax

Section 541 of the Internal Revenue Code imposes a corporate level penalty tax of 15%¹ on the undistributed personal holding company (“PHC”) income of a PHC. The purpose of the PHC tax regime² is to prevent individuals from avoiding the individual income tax

¹ This rate is scheduled to return to the highest individual tax rate when the lower dividend tax rate expires.

² Sections 541 – 547 of the Internal Revenue Code of 1986.

on interest, dividends, rents and similar types of income by holding investments through corporations. A corporation constitutes a PHC if 60% of its adjusted gross income is PHC income and if 50% of its stock is owned by five or fewer individual shareholders at any time during the last half of the taxable year. PHC income generally is defined as interest, dividends, royalties, rents, and certain other types of passive investment income.

It is important to understand the roots of the PHC tax regime to appreciate why it needs to be reconsidered. In the 1930s the corporate tax rate was 13.5% and the top individual income tax rate was 63% (a 49.5% differential between the top corporate and individual tax rate). Also, pursuant to the so-called *General Utilities*³ doctrine, corporations could liquidate and distribute to their shareholders appreciated assets tax-free. These two factors created incentives for individuals to incorporate their portfolio investments (so-called “incorporated pocket-book”). Congress responded to this situation appropriately by enacting the PHC tax provisions as part of the Revenue Act of 1934.

As the Committee knows full well, the nation’s tax laws have changed significantly since the mid-1930s.

The policy rationales that led to the PHC tax regime are no longer operative. First, the top marginal tax rate for both individuals and corporations is 35%.⁴ Second, corporate liquidating distributions of appreciated assets are taxed at the corporate level. ***Simply put: Today’s tax laws do not provide an incentive to incorporate portfolio investments to escape the individual income tax.***

Application of PHC tax to Carrix

An example will help to clarify the lack of a compelling policy justification for the application of the PHC tax. In the case of a group of corporations filing a consolidated return, the PHC test is generally conducted on the basis of the operations of the consolidated group. However, in certain circumstances the test must be conducted on a separate company basis. When the test is conducted on a separate company basis, a group of corporations filing a consolidated return can easily find that it has a personal holding company tax liability even though a great majority of its revenue is generated from the active conduct of its trade or businesses.

The requirement to conduct the PHC tests on a separate company basis often unfairly penalizes corporate groups that are actively engaged in business. A common fact pattern that gives rise to this unwarranted imposition of the PHC tax is where a member of the group receives dividends from controlled foreign subsidiaries. ***In this case, the separate company PHC tax computation serves as a deterrent to the repatriation and reinvestment of foreign earnings in the United States.***

³ *General Utilities & Operating Company v. Helvering*, 296 U.S. 200 (1935). The *General Utilities* doctrine was repealed by Congress in 1986.

⁴ The top individual tax rate is slated under current law to rise to 39.6% on January 1, 2013 – resulting in less than a 5% differential between the top corporate and individual rates.

In other words, Carrix would be hit by the PHC tax to the extent it repatriated dividends from its overseas affiliates simply because it is a closely held company. If Carrix were organized as a public company, the PHC penalty tax would not apply. Simply because Carrix is closely held, the tax rate on foreign earnings repatriated back to the United States would be, rather than the normal 35% rate, a 50% tax rate. Such a level of tax makes it more economical for Carrix to keep foreign earnings offshore for purposes of further developing international operations, rather than repatriating earnings from overseas operations to fund productive investments in the United States – in Carrix’s case, for example, we would plan to use the repatriated cash to fund an expansion of a major port terminal facility in Washington state.

Additional Policy Considerations

Carrix believes that additional policy considerations argue in favor of repealing, or substantially modifying, the PHC tax regime. The tax was enacted to prevent affluent individuals from escaping the reach of the individual income tax. Given the changes described above in the overall design elements of our nation’s tax law today, in practice, the PHC tax regime does less to deter the formation of so-called “incorporated pocketbooks” than to inhibit closely-held active businesses with less than six shareholders from pursuing logical business transactions that other companies are able to do because they may give rise to PHC tax consequences.

While some companies are able to evade the reach of the PHC tax through sophisticated tax counsel, other companies are not so lucky and are either unaware of the PHC tax or cannot avoid the tax unless they change their ownership structure. In addition, the PHC tax adds significant complexity to the Internal Revenue Code while raising a relatively nominal amount of tax revenue: approximately \$10 million per year.⁵

Most importantly, from our perspective, the PHC tax unnecessarily and unfairly taxes revenues which would otherwise be available for investment in much needed infrastructure projects or other important corporate uses which would promote economic development in the United States.

Conclusion

Thank you for the opportunity to submit these written comments for the record. Carrix looks forward to working with you and your staffs to ensure that the U.S. tax code is reformed in a way that makes sense and that, in particular, removes this one particular piece of tax legislative “dead wood” from the Code.

⁵ Corporation Income Tax Returns, 2002 (IRS SOI Bulletin, 2005).